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IN THE

Supreme Court of the United States

REYNOLDS METALS COMPANY, *Appellant,* v. THE STATE OF WASHINGTON, et al., *Appellees.*	No.....

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF WASHINGTON

JURISDICTIONAL STATEMENT

Reynolds Metals Company (hereinafter referred to as "Reynolds") has appealed from the Final Judgment of the Supreme Court of the State of Washington entered April 19, 1965, and submits this Statement to show that this Court has jurisdiction of this appeal and that the questions presented are constitutionally substantial and of public importance.

The Appellees are the State of Washington and the Tax Commissioners of the State of Washington.

OPINIONS BELOW

The opinion of the Supreme Court of the State of Washington is reported at 65 Wn.2d 855, 400 P.2d 310 (Appendix "A"). The trial court's opinion (Superior Court of Thurston County, Washington) is unreported (Appendix "B").

JURISDICTION

Reynolds brought suit under Section 82.32.180 of the Revised Code of Washington in the Superior Court for the recovery of business and occupation tax imposed on the privilege of manufacturing. The tax was assessed on the basis of *total value* of aluminum ingots produced at Reynolds' Washington plant, notwithstanding that said aluminum had been produced as a result of activities carried on in successive stages in several states which culminated in the production of said ingots in the State of Washington. All of said aluminum was subsequently shipped out of the state, in small part for sale, but largely for manufacture by Reynolds into fabricated items. The taxes for the year 1955 were selected by agreement of the parties as being imposed with respect to a representative year, refund for prior or subsequent years to be held in abeyance pending outcome of the litigation.

The Superior Court denied recovery and the State Supreme Court affirmed by Final Judgment entered April 19, 1965 (Appendix "C").

Notice of Appeal to this Court was filed in the State Supreme Court on July 13, 1965. Jurisdiction of this Court is conferred by 62 Stat. 929, 28 U.S.C. No. 1257(2). The following cases sustain such jurisdiction: *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450; *Field Enterprises, Inc., v. State of Washington*, 352 U.S. 806; *Gwin, White & Prince, Inc., v. Henneford, et al.*, 305 U.S. 434; *Dahnke-Walker Milling Company v. Bondurant*, 257 U.S. 282.

QUESTIONS PRESENTED

The State of Washington imposes an *unapportioned* tax on the privilege of manufacturing within said State which is measured by the *total* value of the item at the stage of production reached in said State.

The following questions are presented by this appeal:

1. Is manufacturing a "purely local activity" and hence not protected by the Fourteenth Amendment or the Commerce Clause of the United States Constitution?

2. Does the Fourteenth Amendment and the Commerce Clause of the United States Constitution prohibit an additional tax burden imposed solely because an interstate business manufactures items in successive stages in several states rather than performing all manufacturing in one state?

3. When the item has been produced partly without said State and thereafter partly within said State, is the effect of said unapportioned tax so measured to impose a tax upon activities outside the State and, therefore, is the tax repugnant to the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States?

4. Is the Washington tax so seriously at variance with the taxing system of other states as to create substantial dangers of multiple burdens prohibited under the Commerce Clause?

5. Is said Washington tax, which exempts from the tax on manufacturers those who pay the tax as sellers, repugnant to the Commerce Clause of the United States

Constitution and to the Fourteenth Amendment when applied to the production of an item in successive stages without and within said State for shipment outside the State, since it provides only a single tax on a combination of local manufacture and local sale while subjecting a combination of local manufacture and subsequent out-of-state further manufacture and/or sale to further taxation?

STATUTES AND CONSTITUTIONAL PROVISIONS

The tax here involved was imposed by Sections of Title 82, Chapter 82.04 of the Revised Code of Washington. Pertinent Sections, or portions thereof, of the tax statute are set forth in Appendix "D."[1]

Article I, Section 8, Clause 3, of the Constitution of the United States (Commerce Clause) and the Due Process and Equal Protection Clauses of the Fourteenth Amendment to that Constitution here invoked are set forth in Appendix "E."

STATEMENT OF THE CASE

This was an appeal from the denial of refund of taxes, purportedly imposed for the privilege of "engaging within this state (Washington) in business as a manufacturer" (RCW 82.04.240) measured by the unapportioned and total value of a product (aluminum ingots) resulting from production activities carried on in several states as hereinafter described, and which, even in that stage (ingots), was largely for ultimate fabrication in other states by Reynolds.

1. RCW 82.04.220; RCW 82.04.240; RCW 82.04.270; RCW 82.04.440.

Reynolds is a Delaware corporation and is engaged principally in the production and sale of aluminum and aluminum products. It is an integrated producer whose manufacturing activities occur in four principal stages: (1) Mining and treatment of bauxite, (2) Producing alumina from bauxite, (3) Reducing aluminum metal from alumina, (4) Fabricating the raw metal into various aluminum products, such as plate, sheet, foil, rod, bar, etc.

All of Reynolds' U. S. bauxite operations were in Arkansas. There was no mining or processing of bauxite by anyone in the State of Washington. Its plants for the production of alumina from bauxite were in Arkansas and Texas. There was no production of alumina in Washington. Therefore, all alumina used at Reynolds' plant is obtained from other plants of Reynolds. Reynolds' plants to reduce alumina to aluminum were in Texas, Arkansas, Alabama, Oregon and Washington. It did no other manufacturing in Washington. Reynolds' plants to fabricate aluminum ingots into various end items were in several states, including Illinois, Alabama, Arizona, Kentucky, Virginia and New Jersey.

The various production activities were performed in said several states as follows:

Bauxite is mined, then processed and transported to Reynolds' alumina plants in Arkansas and Texas. Alumina is produced from the bauxite by an extensive process known as the Bayer Process.[2]

2. The Bayer Process involves three basic procedures described in detail in Ex. 3, p. 10 (R. 128).

Reduction of alumina to metallic aluminum is achieved at the Washington plant by the Hall Reduction Process. The greater part of the ingots resulting from this reduction process were shipped from Reynolds' Washington plant to Reynolds' fabricating plants outside of Washington. Some ingots were sold *outside* Washington to customers located *outside* of Washington. At Reynolds' fabricating plants the aluminum was manufactured into various end products and to do so the ingots were remelted, alloyed and then cast into sheet ingots or extrusion billets.

Various items used in the reduction process in Washington are produced at other plants by Reynolds.[3] These items were subject to tax in the states where they were processed. For example, in the State of Arkansas, which was the principal source of the alumina which was shipped to the Washington plant, the manufacture of alumina was subject to tax. The plant at Longview is wholly dependent upon the other plants of Reynolds described above, for its operation; it is dependent upon the alumina plants for the production of alumina and it would not be in business if it did not have the fabricating plants to which it could ship the aluminum ingots for fabrication.

In the year 1955, Reynolds disposed of the product of its Washington plant as follows: 81.17 per cent transferred to other Reynolds plants outside Washington for

3. Aluminum fluoride in the plant in Arkansas; potlining mix in the plant in Oregon; aluminum sheet casing in the Illinois or Alabama plant; bath skimmings in the plant in Oregon; carbon butts in the Oregon plant.

use in further manufacturing; 18.83 per cent sold to customers outside Washington.

Costs to the Longview plant were recorded in its books of account for products produced in Reynolds' plants outside Washington and transferred to Washington for further processing. Said costs were recorded on the Washington plant as interdepartmental charges to that plant by Reynolds' plants outside Washington.[4]

HOW THE FEDERAL QUESTIONS WERE RAISED IN PROCEEDINGS BELOW

The federal questions sought to be reviewed were raised in the Superior Court by the Notice of Appeal and Complaint, prayer for injunction, Appellant's Proposed Findings of Fact and Conclusions of Law, and the Findings of Fact and Conclusions of Law entered by the Superior Court (R. 30), and were fully argued and briefed before that Court. The Superior Court held that the Washington tax on manufacturing made no provision for apportioning its base and denied Appellant's claim that the unapportioned tax was repugnant to the Commerce Clause

4. Production costs for products produced in Reynolds' plants outside Washington for the year 1955 were:

Alumina	$7,377,817
Aluminum Fluoride	164,997
Potlining Mix	84,030
Aluminum Sheet Casing	55,336
Bath Skimmings	19,886
Carbon Butts	11,998
Miscellaneous	420
	$7,714,484

Total manufacturing costs recorded on Washington plant books were $15,794,570; the balance of $8,080,086 was for local manufacturing costs. The local costs were, therefore, .511574 of the total cost of $15,794,570.

of, and the Due Process and Equal Protection Clauses of the Fourteenth Amendment to, the United States Constitution. On appeal, the State Supreme Court affirmed the Judgment of the Superior Court.

The federal questions were raised in the State Supreme Court by Assignments of Error in Appellant's brief and were fully argued and briefed. The opinion of that Court (Appendix "A") shows that the federal questions were raised and decided as necessary grounds for its judgment and that the validity of the tax statute as applied was drawn in question and sustained against claims of repugnancy to the United States Constitution. This case is within the requirements for appeal jurisdiction as set forth in *Dahnke-Walker Milling Company v. Bondurant*, 257 U.S. 282. *Field Enterprises, Inc., v. State of Washington*, 352 U.S. 806, and *Gwin, White & Prince, Inc., v. Henneford, et al.*, 305 U.S. 434, were appeals from the same state court involving the same tax. This Court, accordingly, has jurisdiction on appeal pursuant to 62 Stat. 929, 28 U.S.C. § 1257(2).

THE QUESTIONS ARE SUBSTANTIAL

First Question

"Is manufacturing a 'purely local activity' and hence not protected by the Fourteenth Amendment or the Commerce Clause of the United States Constitution?"

The Supreme Court of Washington did not question in its opinion (Appendix "A") the existence of the multiple burden on Reynolds' or the inclusion in Reynolds' tax base of amounts attributable to manufacturing

activities outside Washington, each established by the evidence and fully briefed and argued. It merely held that the multiple burden and extraterritorial tax base were effectively immaterial because manufacturing is a "purely local activity" and hence not entitled to any of the protection afforded an interstate business by the Fourteenth Amendment or the Commerce Clause (Art. I § 8, Clause 3) of the Constitution:

> "Reynolds contends that the tax imposed offends the Fourteenth Amendment to the federal constitution [because it is] a tax on extraterritorial activities and values. We discussed this argument at length in *Crown Zellerbach Corp. v. State, supra* (53 Wn.2d 813) . . . Here, the tax on Reynolds is for *a purely local activity.* Neither the Fourteenth Amendment to the federal Constitution nor [the Washington Constitution] is contravened.
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> "Reynolds further contends that since the tax imposed is not apportioned, it places a multiple burden upon, or directly interferes with, interstate commerce, in violation of the commerce clause of the federal Constitution, Art. 1, § 8, Clause 3. This argument is answered by our holding in *Crown Zellerbach Corp. v. State, supra,* 53 Wn.2d 813. The *tax on the local activity of manufacturing does not transcend state lines.*" (Emphasis added) (Appendix A, p. 6,7)

The Washington Court continues to espouse the view, erroneously considered to accord with decisions of the Supreme Court of the United States, that manufacturing is *per se* a local activity. It is following and citing as current law a line of cases which, in Justice Jackson's phrase in *Wickard, et al. v. Filburn,* 317 U.S. 111 (1942), was "superseded" (p. 122) years ago. Its error is evident from the following comparison of (A) the author-

ities relied upon in the *Crown Zellerbach* cases, 45 Wn. 2d 749, 278 P.2d 305, and 53 Wn.2d 813, 328 P.2d 884, which latter cases the Supreme Court of Washington cites in Appendix "A" as the basis for its decision here under appeal, with (B) the characterization of these same authorities in *National Labor Relations Board v. Jones & Laughlin Steel Corporation*, 301 U.S. 1, and *Wickard, et al. v. Filburn, supra:*

(A) Supreme Court of Washington

In the *Crown Zellerbach Corporation v. State* cases, *supra*, the Washington court said (emphasis added):

> "The tax with which we are concerned is a tax on the privilege of manufacturing and extracting. *The United States Supreme Court has repeatedly held that manufacturing is not a part of interstate commerce. In Utah Power & Light Co. v. Pfost*, 286 U.S. 165, 52 S.Ct. 548, 552, 76 L.Ed. 1038, the Supreme Court said:
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> "'. . . that commerce does not begin until manufacture is finished, and hence *the commerce clause of the Constitution does not prevent the state from exercising exclusive control over the manufacture. Cornell v. Coyne*, 192 U.S. 418, 428, 429, 24 S.Ct. 383, 48 L.Ed. 504. "Commerce succeeds to manufacture, and is not a part of it." *United States v. E. C. Knight Co.*, 156 U.S. 1, 12, 15 S.Ct. 249, 253, 39 L.Ed. 325 . . .'
>
> "Similarly the activity of extracting is not in interstate commerce. *Oliver Iron Mining Co. v. Lord*, 262 U.S. 172, 43 S.Ct. 526, 67 L.Ed. 929 . . . (45 Wn.2d 759-760).
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> . . .
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> "'. . . in the case presently before us, *the incident upon which the tax is imposed, that is, manufacturing, is purely a local activity and, hence, properly*

taxable. . . . Utah Power & Light Co. v. Pfost, 1932, 286 U.S. 165, 52 S.Ct. 548, 76 L.Ed. 1038." (53 Wn. 2d 816)

(B) Supreme Court of the United States

National Labor Relations Board v. Jones & Laughlin Steel Corporation, supra, made it plain that the cases on which the Washington Court now relies were *not* authority for any proposition that manufacturing is local *per se*:

> "Respondent says that whatever may be said of employees engaged in interstate commerce, the industrial relations and activities in the manufacturing department of respondent's enterprise are not subject to federal regulation. *The argument rests upon the proposition that manufacturing in itself is not commerce. . . . Oliver Iron Co. v. Lord*, 262 U.S. 172, 178, 43 S.Ct. 526, 67 L.Ed. 929. (p. 34)
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> "The close and intimate effect which brings the subject within the reach of federal power may be due to activities in relation to productive industry although the industry when separately viewed is local. (p. 38)
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> "In the *Standard Oil* and *American Tobacco* cases . . . [c]ounsel relied upon the decision in *United States v. E. C. Knight Co.*, 156 U.S. 1 . . . the court summarily dismissed the contention in these words: 'But all the structure upon which this argument proceeds is based upon the decision in *United States v. E. C. Knight Co.*, 156 U.S. 1, 15 S.Ct. 249, 39 L.Ed. 325. The view, however, which the argument takes of that case, and the *arguments based upon that view* have been so repeatedly pressed upon this court in connection with the interpretation and enforcement of the Antitrust Act, and *have been so necessarily and expressly decided to be unsound as*

to cause the contention to be plainly foreclosed and to require no express notice' (citing cases)." (Emphasis added) (pp. 38, 39)

If any doubt remained in 1937 after *Jones & Laughlin* as to whether manufacturing might still be considered local *per se*, it was removed in 1942 in *Wickard, et al. v. Filburn, supra*, which categorized as "superseded" the view of the self-same cases *(Utah Power & Light Co. v. Pfost, supra, et al.)* (See 317 U.S. at 121 and N. 21) which the Supreme Court of Washington still cites as authority for its view that manufacturing is a "purely local activity":

> "The government's concern . . . is attributable to a few dicta and decisions of this court which might be understood to lay it down that activities such as 'production,' 'manufacturing' and 'mining' are strictly 'local' . . . [footnote 21 cross reference to *Utah Power & Light Co. v. Pfost, supra; Oliver Iron Mining Co., supra, inter alia]* . . . Certain activities such as 'production,' 'manufacturing' and 'mining' were occasionally said to be within the province of state governments and beyond the power of Congress under the Commerce Clause. (317 U.S. at 119-121)
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> "When it first dealt with this new legislation, the Court adhered to its earlier pronouncements and allowed but little scope to the power of Congress. *United States v. E. C. Knight Co.*, 156 U.S. 1, 15 S.Ct. 249, 39 L.Ed. 325. These earlier pronouncements also played an important part in several of the five cases in which this Court later held that Acts of Congress under the Commerce Clause were in excess of its power. [Footnote reference to *Oliver Iron Co. v. Lord*, 262 U.S. 172, 178, 179, 43 S.Ct. 526, 529, 67 L.Ed. 929; *Utah Power & Light Co. v. Pfost*, 286 U.S. 165, 52 S.Ct. 548, 76 L.Ed. 1038.] (317 U.S. at 121-122)

"Even while important opinions in this line of restrictive authority were being written, however, *other cases called forth broader interpretations of the Commerce Clause destined to supersede the earlier ones, and to bring about a return to the principles first enunciated by Chief Justice Marshall in Gibbons v. Ogden, supra.*

"Not long after the decision of *United States v. E. C. Knight Co., supra,* Mr. Justice Holmes, in sustaining the exercise of national power over intrastate activity, stated for the Court that 'commerce among the states is not a technical legal conception, but a practical one, drawn from the course of business.' *Swift & Co. v. United States,* 196 U.S. 375, 398, 25 S.Ct. 276, 280, 49 L.Ed. 518." (317 U.S. 122) (Emphasis added)

In Volume I of *A Commentary On the Constitution of the United States* (Macmillan, 1963), Dr. Barnard Schwartz (Professor of Law, New York University) summarizes at page 186 the 19th century view, still being adhered to by the Supreme Court of Washington:

"The result [of viewing manufacturing as a 'purely local activity'] was the artificial and mechanical separation of 'manufacturing' from 'commerce,' without regard to their economic continuity or the effects of the former upon the latter. Manufacture itself was treated as a 'purely local' activity and hence beyond the compass of the Commerce Clause.

"What was true of manufacturing was also true of all other forms of 'production.' 'Commerce,' stated the high court in *Knight,* 'succeeds to manufacture, and is not a part of it.' The same can be said of agriculture, mining, and every other means by which goods are produced. In *Oliver Iron Co. v. Lord* (1923), the court expressly applied the *Kidd-Knight* approach to the mining of iron ore. 'Mining,' said the court, 'is not interstate commerce but, like man-

ufacturing, is a local business, subject to local regulation and taxation.'

"Later cases applied the same reasoning to agriculture, oil production, generation of electric power, and other productive industries. All of these activities were held beyond the reach of the Congressional commerce power, although they, together with manufacturing, constituted the heart of the economic life of the country."

In the same Commentary, Professor Schwartz describes the transition to the modern concept of manufacturing as a part of interstate commerce (pp. 198-199):

". . . The *Jones & Laughlin* decision marks a definite break with the restricted view that productive industries are beyond the scope of the Commerce Clause. In *Jones & Laughlin*, the Supreme Court held squarely that manufacturing as such was not automatically excluded from the range of federal power.

* * *

"It is thus clear that, under the view that has prevailed in the highest court since the *Jones & Laughlin* case, productive industries such as manufacture and agriculture are no longer removed from the reach of the commerce power. *No longer must production be treated as a purely 'local' activity,* immune from Congressional control regardless of the impact which it may have upon the commerce of the country. Instead, we have come back to the Marshall conception of commerce as an organic whole, with the Commerce Clause embracing all commerce which concerns more than one state. Under such conception, *the federal power* is not limited to commerce which actually moves across state lines. It *includes all activities which affect interstate commerce, though such activities, taken alone, might be considered 'local.'*" (Emphasis added)

Second Question

"Does the Fourteenth Amendment and the Commerce Clause of the United States Constitution prohibit an additional tax burden imposed solely because an interstate business manufactures items in successive stages in several states rather than performing all manufacturing in one state?"

In 1963 and again in 1965 the Supreme Court of the United States, in invalidating a Louisiana use tax and a District of Columbia income and franchise tax, emphasized as a basis for its decisions the economic fragmentation that would have resulted from the taxes that were held invalid:

> "At best, this would encourage the appellant to locate his assembly operations in the state of largest use for the units. At worst, it would encourage their actual fractionalization or discontinuance. Clearly, approval of the Louisiana use tax in this case would 'invite a multiplication of preferential trade areas destructive . . . of the very purpose of the Commerce Clause'". *Halliburton Oil Well Cementing Co. v. Reily,* 373 U.S. 64, 72, 73.

> ". . . the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location . . ." *General Motors Corp. v. District of Columbia,* 380 U.S. 553, 560.

Exactly the same sort of economic fragmentation, either fortuitously or by design, is implicit in the unapportioned Washington tax on the privilege of manufacturing. Although the tax differs in name from the use tax in *Halliburton* and the income and franchise tax in *General Motors Corp.*, its practical operation and

effect is the same; the description pigeonhole is immaterial (*Halliburton, supra; Wisconsin, et al., v. J. C. Penney Co.*, 311 U.S. 435, 443). Certainly a state cannot be allowed to escape Constitutional requirements for apportionment by measuring the tax by gross income or value (equated in RCW 82.04.070, 82.04.080, and 82.04.090), less more limited deductions (RCW 82.04.430) than normally allowed in a net income tax, compensating for the restricted pattern of deductions by lowering the tax rate, and then claiming it has avoided the Constitutional necessity for apportionment.

The comparison of the tax burden on a local manufacturer who completes all his manufacturing processes in one state and an interstate manufacturer who produces an identical finished product in successive manufacturing stages in several states is illustrated in Appendix "F". At the first production stage (here, "bauxite"), the tax as paid by either a local or an interstate manufacturer is identical—$20,000 in the example. Thereafter, the unapportioned tax base on the interstate manufacturer pyramids, ultimately resulting in $156,000 of additional tax, or 93 per cent more than paid by a local manufacturer.

The multiple tax burden inevitably discourages interstate shipments and encourages performance of all manufacturing operations within a single taxing jurisdiction to avoid a pyramided tax base. Reynolds, according to the State's taxing theory, solely because it manufactures in successive stages in several states can be taxed on an overlapping and unapportioned tax base in the states

where the bauxite is extracted, where the alumina is produced, where the primary aluminum (ingot) is produced, where the aluminum is fabricated and where the product is finally sold. Obviously, if an interstate manufacturer is to compete with a local manufacturer, it can do so effectively only by having all its manufacturing operations in a single state and discontinuing interstate transfers of semi-fabricated products which an economic pattern of plant location would otherwise dictate.

Performing the same manufacturing activities, incurring the same before-tax costs, and completing products having identical values, Reynolds' interstate business would pay manufacturing taxes under the computational method required by Washington in almost double the amount paid by a local manufacturer confining the same business to Washington. Moreover, it is obvious from Appendix "F" that the extent of the cumulative burden is proportional to the number of taxing jurisdictions among which the manufacturer divides its operations, to the magnitude of the out-of-state activities, and to the purely fortuitous circumstance as to the manufacturing stage [high or low value] at which semi-finished goods are transferred from one state to another. Thus, interstate business is required to pay a heavy tax penalty for the interstate privilege, the more extensive its interstate nature then the heavier the penalty—a glaring instance of the discrimination and local favoritism against which the Commerce Clause has historically afforded protection.

Mr. Justice Jackson, speaking for the Court, in *H. P.*

Hood & Sons, Inc., v. Du Mond, 336 U.S. 525, stated (at pp. 538-539):

> "The material success that has come to inhabitants of the states which make up this federal free trade unit has been the most impressive in the history of commerce, but the established interdependence of the states only emphasizes the necessity of protecting interstate movement of goods against local burdens and repressions . . . What fantastic rivalries and dislocations would ensue if such practices were begun!"

The Constitutional infirmity of the multiple burden and the extraterritorial tax base can be remedied only by apportionment, for only after such apportionment will the two curves on Appendix "F" approximate each other. In *General Motors Corp. v. Washington et al.*, 377 U.S. 436, the need for apportionment of the Washington business and occupation tax in appropriate circumstances was once again emphasized, and the Court pointed out that Washington's unapportioned tax was by its very nature suspect:

> ". . . local taxes measured by gross receipts from interstate commerce have not always fared as well. Because every state has equal rights when taxing the commerce it touches, there exists the danger that such taxes can impose cumulative burdens upon interstate transactions which are not presented to local commerce [citations]. Such burdens would destroy interstate commerce and encourage the reerection of those trade barriers which made the Commerce Clause necessary . . . interstate commerce cannot be subjected to the burden of 'multiple taxation' . . . taxation measured by gross receipts is constitutionally proper if it is fairly apportioned. (377 U.S. at 440)

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"[The Washington tax] is unapportioned and, as we have pointed out, is, therefore suspect." (377 U.S. at 448)

The result in the *General Motors* case, *supra*, is irrelevant, or in any event not controlling here. There it was held that an unconstitutional burden had not been shown.[5] However, it has been shown here by specific proof of the activities in other states which contributed to the value taxed here and the impact of taxes imposed in other states on those activities. Furthermore, no claim for apportionment was before the court in *The General Motors* case, *supra*. However, it was claimed here and the basis therefore proved. The Constitutional importance of apportionment has been so well recognized by this Court (most recently in the foregoing case) when the Washington business and occupation tax was last before this Court, that no elaboration is required of the substantial importance of the federal question here raised.

The Supreme Court of Washington, having held in this case that apportionment is not available under the Washington statute, the entire tax is invalid:

"If the statute is inseparable, then both by its terms and its legal operation and effect this tax is

5. "The Court touched upon the problem of multiple taxation in *Northwest Airlines v. Minnesota, supra*, 322 U.S. at 295, 88 L. ed. at 1286, but laid it to one side as 'not now before us.' Thereafter, in *Northwestern States Portland Cement Co. v. Minnesota, supra*, 358 U.S. at 463, 3 L. ed. 2d at 430, we held that 'in this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense.' Appellant has not done this. It has not demonstrated what definite burden, in a constitutional sense, the St. Louis tax places on the identical interstate shipments by which Washington measures its tax." *General Motors Corporation v. Washington*, 377 U.S. 436 at 449.

imposed generally upon the entire business conducted, including interstate commerce as well as domestic, and the tax is void . . ." *Bowman v. Continental Oil Company*, 256 U.S. 642, at 647.

"It is because the tax, forbidden as to interstate commerce, reaches indiscriminately and without apportionment, the gross compensation for both interstate commerce and intrastate activities that it must fail in its entirety so far as applied to receipts from sales interstate." *J. D. Adams Manufacturing Co. v. Storen*, 304 U.S. 307, at page 314.

The Supreme Court of Washington has simply failed to take cognizance of and give effect to the modern and current position of this Court. The error of the Washington Court is material and the Federal question substantial. The case involves not only the tax for the test year here involved, but also will determine whether approximately one million dollars in taxes for other years will be refunded to Reynolds. It will indirectly determine the state taxing basis of the entire Washington aluminum industry and of other interstate manufacturers having similar successive stages of production. And it will decide whether states can hobble interstate commerce by taxation or otherwise by simply dubbing the activities "manufacturing," and applying as a rule of law a concept which the Supreme Court of the United States since 1942 has held to be "superseded."

Third Question

"When the item has been produced partly without said State and thereafter partly within said State, is the effect of said unapportioned tax so measured to impose a tax upon activities outside the State and, there-

fore, is the tax repugnant to the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States?"

The unapportioned tax is, in effect, imposed on extra-territorial activities and constitutes the denial of due process of law guaranteed by the Fourteenth Amendment to the Constitution of the United States.

The power of a state to impose a privilege tax exists only with respect to privileges exercised by the taxpayer within the state. The extent of Reynolds' extraterritorial activities that have been included in the Washington tax base has been shown in this case by the out-of-state costs (see note 4, page 7) incurred in the production of aluminum.

When the taxpayer is a foreign corporation engaging in multi-state activities as a part of its manufacturing process, and the tax on the privilege of manufacturing is measured by activities performed partly within the state and partly without the state, it should be clear that some fair and reasonable apportionment is necessary or the tax will be invalid because asserted on activities beyond the taxing jurisdiction of the state.

In the case of an integrated manufacturing business such as Reynolds, when manufacturing activities within a state are absolutely dependent upon those outside, the question becomes primarily an accounting problem in computing a fair apportionment factor that can be applied to an aggregate amount to determine that segment which is reasonably attributable to local activities and,

therefore, taxable by the state in which such activities are carried on. While this Court has stated that mathematical precision cannot be expected of any apportionment system, it is equally clear that a valid apportionment system must not operate extraterritorially in attributing to the state a percentage of activity out of all proportion to the business transactions carried on within the state. A landmark opinion setting forth this general principle is *Hans Rees' Sons, Incorporated v. North Carolina*, 283 U.S. 123, which stated:

> "When, as in this case, there are different taxing jurisdictions, each competent to lay a tax with respect to what lies within, and is done within, its own borders, and the question is necessarily one of apportionment, evidence may always be received which tends to show that a state has applied a method, which, albeit fair on its face, operates so as to reach profits which are in no just sense attributable to transactions within its jurisdiction." (p. 134)

If the practical operation and effect of the tax is to expose extraterritorial values or activities to a tax burden, such a tax is invalid regardless of its descriptive pigeonhole.[6]

The unconstitutionality of this tax as applied has been indicated by *Halliburton Oil Well Cementing Com-*

6. "But the descriptive pigeon-hole into which a state court puts a tax is of no moment in determining the constitutional significance of the exaction. 'In whatever language a statute may be framed, its purpose must be determined by its natural and reasonable effect' (citations). Such has been the repeated import of the cases which only recently were well summarized by the guiding formulation for adjudicating a tax measure, that 'in passing on its constitutionality we are concerned only with its practical operation, not its definition or the precise form of descriptive words which may be applied to it.' (citations)." *Wisconsin, et al., v. J. C. Penney Co.*, 311 U.S. 435, 443, 444.

pany v. Reily, 373 U.S. 64 (1963), holding invalid a tax that imposed a greater tax burden solely because property was transferred from out of state. While the Louisiana tax was denominated a use tax rather than a business and occupation tax, the court made clear that it was not concerned with appellations but with the practical operation and effect of a tax.[7]

Thus it is of no moment that two taxes are differently denominated if they possess similar constitutional infirmities.

Appendix "F" illustrates the differences in the Washington tax burden which arise solely because an enterprise transfers semi-finished goods interstate for further processing, rather than performing the entire manufacturing and selling process within Washington.

The effect of the multiple burden imposed on interstate manufacturers by Washington, like that of Louisiana, is to reduce interstate shipments and to encourage performance of all manufacturing operations within a single taxing jurisdiction in order to avoid a pyramided tax base. Obviously, if an interstate manufacturer is to compete with a local manufacturer, it can do so effectively only by having all its manufacturing operations in a single state and discontinuing interstate transfers of semi-

7. "This is another in a long line of cases attacking state taxation as unduly burdening interstate commerce. As this court stated in *Best & Co. v. Maxwell*, 311 U.S. 454, 455-456: 'In each case it is our duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against interstate commerce.' This concern with the actuality of operation, a dominant theme running through all state taxation cases, extends to every aspect of the tax operations." *Halliburton Oil Well Cementing Company v. Reily*, 373 U.S. 64, 69 (1963).

fabricated products. (See quotation from the *Halliburton* case at page 15, *supra.*)

Fourth Question

"Is the Washington tax so seriously at variance with the taxing system of other states as to create substantial dangers of multiple burdens prohibited under the Commerce Clause?"

In *General Motors Corp v. District of Columbia, supra,* the Court noted that a taxing system seriously at variance with those of other states created a substantial risk of multiple burden:

> ". . . approval of the District Commissioner's regulations lends sanction to an apportionment formula seriously at variance with those prevailing in the vast majority of States and creates substantial dangers of multiple taxation." (p. 556, 557)
>
> ". . . the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location, . . ." (p. 560).
> " . . . The conclusion which we draw . . . finds further support in the continuing concern for fair apportionment which this Court has displayed over the years in scrutinizing state taxing statutes." (p. 561, 562)

Although the District of Columbia tax was an income and franchise tax, whereas Washington terms its tax a business and occupation tax, both are measured by income or value less certain deductions (more limited in the case of Washington, but offset in effect by the lower tax rate). More important, both are ostensibly levied for

the same purpose—the privilege of engaging in trade or business in the taxing jurisdiction (D.C. Code, 1961, §47-1571a; RCW 82.04.220 and 82.04.240).

Washington's privilege tax is unapportioned, and the District of Columbia's was apportioned on a one-factor formula. The District of Columbia tax was held invalid as not measuring the income "fairly attributable" to the District and creating a risk of multiple burden. If a one-factor apportionment formula creates a substantial risk of multiple burden, *a fortiori* a "no-factor" formula such as Washington's, i.e., a total lack of any apportionment, where manufacturing has taken place in successive stages in several states, must be even more unacceptable under the multiple burden test whether applied on a statutory (District of Columbia) or Constitutional basis.

The Washington tax is unique: no other state imposes an unapportioned tax of this nature. Other states recognize both the inequity and the essential illegality of an unapportioned activity tax.[8] For example, Arkansas, where Reynolds manufactured most of the alumina processed

8. For example, West Virginia, which imposes a business and occupation tax otherwise comparable to Washington's, apportions the tax on the basis of:

> ". . . that proportion of the sale price of the manufactured product that the payroll cost of manufacturing within this state bears to the entire payroll cost of manufacturing the product; or, at the option of the taxpayer, . . . the proportion of the sales value of the articles that the cost of operation in West Virginia bears to the full cost of manufacture of the articles." (Code of West Virginia, Ch. 11, Art. 13, Sec. 2-b.)

Similarly, Alabama provides in its income tax regulations that:

> ". . . total material used in manufacturing both within and without the state shall be allocated on some equitable basis such as the ratio of direct labor and manufacturing expense within Alabama to the total thereof." (Ala. Reg. 398.2).

Kansas has a substantially identical provision (Reg. Kan. Tax Law, Art. 92-4-87).

at Longview, imposed a tax[9] measured by "the gross income of a taxpayer less the deductions allowed" (Ark. Stats. 1947, 84-2007); gross income less allowable deductions is also the measure of the Washington tax. But Arkansas apportioned its tax on Reynolds by multiplying the aforementioned base by apportionment factors designed to reflect Arkansas activities only, which included activities at the Arkansas plant that manufactured the alumina for further processing in Washington into aluminum. In contrast, Washington included in its tax base not only amounts reflecting activities in Washington, but additional amounts reflecting prior activities in Arkansas (the manufacture of alumina) which were also taxed in Arkansas. Thus, the multiple burden was not merely a risk but an accomplished fact.

Substantially similar taxes to those of Arkansas were imposed in states to which the semifinished goods (ingots) from Washington were transferred for fabricating. Specifically, for 1955 Reynolds paid more than $600,000 in taxes measured by income to States in which substantial portions of the Washington semifinished product were further processed. In each instance, utilizing a conventional 2- or 3-factor formula, these states included in the measure of their tax a portion of the manufacturing and selling activities reasonably attributable to the taxing

9. When originally enacted in 1923, a substantially similar Arkansas tax was specifically denominated a "gross income tax." See Art. 345, Laws 1923.

jurisdiction. But Washington, in its glaringly disparate taxing system taxed the gross amount without apportionment, including in its measure all activities everywhere up to the time of levy. Whether or not Washington can properly do so while other states are required to apportion taxes having essentially the same operation and effect is one of the very substantial Federal questions here raised.

Fifth Question

"Is said Washington tax, which exempts from the tax on manufacturers those who pay the tax as sellers, repugnant to the Commerce Clause of the United States Constitution and to the Fourteenth Amendment when applied to the production of an item in successive stages without and within said State for shipment outside the State, since it provides only a single tax on a combination of local manufacture and local sale while subjecting a combination of local manufacture and subsequent out-of-state further manufacture and/or sale to further taxation?"

In separate sections, the Washington statute levies taxes on the privilege of manufacturing, RCW 82.04.240, and on the privilege of selling at wholesale, RCW 82.04.270 (Appendix D), but specifically exempts from the manufacturing tax any person taxable as a seller as to the same item, RCW 82.04.440. The statute thus insures that any Washington manufacturer who sells in Washington shall

pay no tax on manufacturing, but a Washington manufacturer such as Reynolds who ships its product in interstate commerce must pay the manufacturing tax. In other words, Appellant is arbitrarily discriminated against because it sells or ships its products in interstate commerce.

In *Columbia Steel Co. v. State of Washington*, 30 Wn. 2d 658, 192 P.2d 976; 34 Wn.2d 700, 209 P.2d 482, and *Weyerhaeuser Sales Co. v. Tax Commission*, 30 Wn.2d 947, 192 P.2d 979; 34 Wn.2d 927, 209 P.2d 490, cert. den. 339 U.S. 903, the Supreme Court of Washington itself held that an earlier version of this statute (Appendix D) was invalid under the Commerce Clause because it exempted from the wholesalers' tax persons who had paid the tax as manufacturers. Thereafter the Legislature promptly inverted the exemption (Appendix "D"), by exempting from the manufacturers' tax persons who had paid the wholesalers' tax, which inversion was held valid by the Supreme Court of Washington in *Crown Zellerbach Corporation v. State, supra.*

The inversion of the exemption is without substance for the economic effect is precisely the same as in the earlier statute which was held invalid. An interstate manufacturer such as Reynolds would still be subject to two taxes—on manufacturing in Washington and on selling in another state—whereas a local manufacturer would pay only one tax and that not on manufacturing. This is not merely a threat of duplicative taxation but an existing competitive circumstance which significantly disadvantages Reynolds. Reynolds' two principal competitors in the aluminum industry also have reduction plants in Washington, substantially larger in aggregate capacity

(88% of Washington capacity as compared to Reynolds' 12%). Unlike Reynolds these competitors fabricate ingot and sell the fabricated products in Washington, and to that extent escape the manufacturing tax imposed on their primary Washington production. Reynolds is not similarly exempt, and must pay the full manufacturing tax in Washington as well as the equivalent taxes on fabricating and selling in other states. As noted under Question Four, comparable taxes in the states to which the production of Longview was transferred for further fabricating aggregated more than $600,000 for the year here involved.

The Federal question is substantial, striking at the heart of a free economy and actively discouraging multistate business and an advantageous distribution of national resources. Washington is establishing through its unapportioned taxes on interstate commerce a preferential trading area wherein a manufacturer will not be taxed as a manufacturer so long as it sells in the State but will be taxed as a manufacturer if it ships its product in interstate commerce. As Professor Schwartz has indicated such a tax philosophy is the antithesis of the Commerce Clause and raises a substantial Federal question:

> "If the Commerce Clause means anything, it means that interstate commerce may not be taxed to the full limit by every state through which it passes. . . . The basic goal should be to prevent an interstate transaction from being saddled with an aggregate tax burden higher than it would bear if it had taken place in the same volume and

over the same distance within a single one of the pertinent states.

"The goal, in other words, should be to place interstate and local commerce, so far as possible, upon a plane of tax equality. Under this approach, any tax which, if applied generally by the states or their subdivisions, would bear more heavily upon interstate commerce than upon like intrastate commerce should be held invalid." I Schwartz, *A Commentary On The Constitution of the United States.* Macmillan (1963) (p. 291).

It is too well established to require detailed analysis here that a state is without power to levy a discriminatory tax, whether that discrimination is forthright or fortuitous. Even though the tax may superficially appear undiscriminatory in form, if its practical effect is to place interstate business at a competitive disadvantage, it is violative of the Commerce Clause.[10]

Such discrimination is also in violation of the Equal Protection Clause of the Fourteenth Amendment:

"No state shall * * * deny to any person within its jurisdiction equal protection of the laws."

The nature of this constitutional prohibition has been summarized as follows:

"One of the most important limitations upon the taxing power of the states is that requiring taxation

10. The prohibition against discriminatory taxation has been often stated as in the following case:

"But it is enough for present purposes that under the Commerce Clause, in the absence of congressional action, state taxation, whatever its form, is precluded *if it discriminates against interstate commerce* or undertakes to lay a privilege tax measured by gross receipts derived from activities in such commerce which extend beyond the territorial limits of the taxing state." *Gwin, White & Prince, Inc. v. Henneford, et al.*, 305 U.S. 434, 438, 439. (Emphasis supplied)

to be equal and uniform, which is enforced both by the equal protection clause of the Fourteenth Amendment to the Federal Constitution and by specific provisions in the constitutions of most of the states. . . . it is clear that the equal protection clause of the Fourteenth Amendment is applicable to state tax legislation and imposes considerable restraint upon state taxing power."[11] (51 Am. Jur., §§150, 168 and 178.)

The prohibition against tax acts capable of imposing multiple burdens such as demonstrated by the instant case has been frequently stated and made effective.[12]

In addition to the prohibition against discrimination and cumulative burdens, the Commerce Clause prohibits any state tax that interferes directly with interstate commerce.[13] A succinct modern statement of this prohibi-

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11. *Ohio Oil Co. v. Conway*, 281 U.S. 146 ("the states, in the exercise of their taxing power . . . are subject to the requirements of the due process and the equal protection clauses of the Fourteenth Amendment"); *Louisville Gas & E. Co. v. Coleman*, 277 U.S. 32.

12. "If Washington is free to exact such a tax, other states to which the commerce extends may, with equal right, lay a tax similarly measured for the privilege of conducting within their respective territorial limits the activities there which contribute to the service. The present tax, though nominally local, thus in its practical operation discriminates against interstate commerce, since it imposes upon it, merely because interstate commerce is being done, the risk of a multiple burden to which local commerce is not exposed." *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434, at p. 439.

13. The nature of the prohibited interference has been delineated in a long line of cases involving a variety of products and activities. In *Michigan-Wisconsin Pipeline Co. v. Calvert*, 347 U.S. 157, a tax was imposed on gathering natural gas. This court nevertheless held that, because the local activity was so closely related to interstate commerce, the flow of commerce could not realistically be separated from the local activity and the tax as applied to such activity interfered with interstate commerce. In *Fisher's Blend Station, Inc. v. Tax Commission*, 297 U.S. 650, a tax was imposed by Washington on generating and transmitting electromagnetic waves. Because the tax was not properly apportioned to intrastate activities, seeking to tax both the apparently local activity of

tion is in *Freeman v. Hewit*, 329 U.S. 249.[14]

As recently as 1959, this Court reaffirmed all three aspects of the Commerce Clause prohibitions by emphasizing in *Northwestern States Portland Cement Co. v. Minnesota* and *Williams v. Stockham Valves and Fittings, Inc.*, 358 U.S. 450, that its decision in those cases was in no way detracting from long-established doctrine as regards direct interference, multiple burdens and discriminations.

CONCLUSION

The above-stated questions and the presentation in support of them demonstrate that this case presents an outstanding and appropriate opportunity for this Court to rule on the effect of the Commerce Clause and the Fourteenth Amendment with respect to the taxation of the large and important segment of industry which requires

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generating, as well as the interstate activity of transmitting, it was held invalid. Similar attempts to interfere directly with interstate commerce rendered the Washington business and occupation tax invalid in *Gwin, White and Prince, Inc. v. Henneford*, 305 U.S. 434. Whether the product or activity relates to natural gas, electromagnetic waves, fruit, or aluminum, the nature of the prohibition is essentially unchanged: in each instance, direct interference with interstate commerce is forbidden and the state is permitted to tax only such part of the activity as is reasonably apportionable to and identifiable with local activities.

14. "A state is also precluded from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between states." (p. 252).... "Nor is there any warrant in the constitutional principles heretofore applied by this court to support the notion that a state may be allowed one single-tax-worth of direct interference with the free flow of commerce. An exaction by a state from interstate commerce falls not because of a proven increase in the cost of the product. What makes the tax invalid is the fact that there is interference by a state with the freedom of interstate commerce • • •." (pp. 256, 257)

for its total performance successive manufacturing steps in several states. The impact of the Washington tax admittedly creates multiple and pyramided burdens which grossly affect and limit the freedom of business and plant location which the Constitution was designed to protect. Appellant respectfully requests this Court to find that these substantial federal questions are entitled to and require plenary consideration.

Respectfully submitted,

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APPENDIX "A"

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

REYNOLDS METALS COMPANY, *Appellant*, v. THE STATE OF WASHINGTON, and WILLIAM HODDE, Chairman, CLARK SQUIRE and G. MERTON DICK, members of the WASHINGTON STATE TAX COMMISSION, *Respondents.*	No. 37426

This is an action by Reynolds Metals Company (hereinafter referred to as Reynolds) to obtain a refund of taxes imposed under the Washington business and occupation tax law. The trial court entered judgment denying the tax refund and injunctive relief requested. Reynolds appeals.

The taxes imposed by the Washington State Tax Commission were for the activities of producing metal aluminum and recovering cryolite at Reynolds' plant in Longview under the classification of manufacturing, pursuant to RCW chapter 82.04.

Reynolds has operations outside the state where bauxite ore is taken from the ground. Alumina is produced from this ore and is shipped to the Washington plant together with cryolite and other materials essential to the aluminum-reduction process, all of which are produced by Reynolds' operations outside the state. From the alumina, pure metallic aluminum pigs or ingots are produced in the Washington plant. A small part of this aluminum is sold outside the state and the remainder is shipped to Reynolds' out-of-state plants for fabrication

into finished aluminum products. Some of the cryolite recovered also is sent to Reynolds' out-of-state plants.

Reynolds contends that it is not a manufacturer of the aluminum metal it ships to its own plants outside of the state for further fabrication because such metal does not constitute an article for "sale" or "commercial or industrial use" essential to the definition of the terms, "manufacturer" and "to manufacture," under RCW 82.04.110 and RCW 82.04.120. None of this aluminum is produced for "sale," as that term is defined in RCW 82.04.140. Reynolds cites RCW 82.04.130:

> ". . . 'Commercial or industrial use' means the following uses of products, including by-products, by the extractor or manufacturer thereof:
>
> "(1) Any use as a consumer; and
>
> "(2) The manufacturing of articles, substances or commodities from extracted products, including by-products."

We are constrained to agree with Reynolds that such activity does not come within the *statutory* definition of "commercial or industrial use," *supra*. First, Reynolds does not use its Longview product, aluminum ingots, as a "consumer" within subsection (1) of RCW 82.04.190. Its use is within the exclusion of subsection (1) (c) therein:

> ". . . 'Consumer' means the following:
>
> "(1) Any person who purchases, acquires, owns, holds, or uses any article of tangible personal property *other than for the purpose . . . (c) of consuming such property in producing for sale a new article of tangible personal property or a new substance,*

of which such property becomes an ingredient or component . . . " (Italics ours)

Second, subsection (2) of RCW 82.04.130 is inapplicable. As contended by Reynolds, it cannot be said that it has produced an extracted product for commercial or industrial use. Reynolds carries on no extracting activity in the state. Only an "extractor" under RCW 82.04.100 produces an extracted product. The production of aluminum is a manufacturing activity and not that of extracting. Neither is the aluminum produced by Reynolds in this state a by-product. RCW 82.04.210.

However, we are not restricted to the *statutory definition* of "commercial or industrial use," in view of RCW 82.04.010, which provides:

> "For the purposes of this chapter, *unless otherwise required by the context*, the terms used herein shall have the meaning given to them in RCW 82.04.020 through 82.04.212." (Italics ours) *St. Paul & Tacoma Lbr. Co. v. State*, 40 Wn.2d 347, 353, 243 P.2d 474 (1952).

Adherence to the statutory definition of "commercial and industrial use" would defeat the paramount intent of the legislature. Reading chapter 82.04 in its entirety, it is evident that the legislature intended therein that all persons engaged in business within the state be subjected to at least one business and occupation tax upon their activities in Washington. This is evident from a reading of RCW 82.04.220, the statute which imposes the tax. It provides:

> "There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities. . . ."

In *Crown Zellerbach Corp. v. State*, 45 Wn.2d 749, 753, 278 P.2d 305 (1954), we emphasized that the legislature intended that business activities within the state be taxed at least once when we said:

> ". . . The legislative purpose, or tax policy, of the above-quoted statutes is to provide for as equitable an imposition of *actual tax liability* as possible in so far as our state business and occupation tax is concerned. Implicit in this policy is the avoidance of an imposition of double or triple tax liability as to particular products. In other words, the policy is to impose *actual liability* for payment of tax only once —on either (a) extracting, or (b) manufacturing, or (c) wholesaling. Thus, actual liability for the payment of the business and occupation tax is the key to the problem. The corollary of this policy is that actual liability for business and occupation tax *be imposed on at least one activity.*"

The term, "commercial or industrial use," as it appears in the definition of "Manufacturer" in RCW 82.04.110 and "To manufacture," in RCW 82.04.120, when considered in context, in light of the legislative intent, clearly requires a different definition of "commercial or industrial use," from that which appears in the statute, namely, the generally recognized definition. See *St. Paul & Tacoma Lbr. Co. v. State, supra.* We need no citation of authority to support our holding that Reynolds' activity in producing aluminum metal ingots in Washington for its subsequent use in fabrication of articles for sale in other states is one for "commercial or industrial use" under the general meaning of that term. The production of aluminum by Reynolds in its Longview plant constituted the activity of manufacturing in the state of Washington under RCW 82.04.120 within the context of the

business and occupation tax statutes.

Reynolds contends, however, that the aluminum metal it ships to its plants out of the state for further fabrication should not be subject to tax, as these deliveries are exempt as "interdepartmental charges" under Rule 201 of the State Tax Commission:

> "In computing tax, *except when the tax is measured by value of products,* there may be excluded or deducted, whichever is applicable, the amounts constituting interdepartmental charges.
>
> "The term 'interdepartmental charges' applies to amounts credited to the sales account or other gross income account of a taxpayer for goods, materials or services furnished by one department or branch of a business organization conducted by a person subject to tax to another department or branch of the same business concern or firm." (Italics ours)

The rule by its exception does not apply to a tax measured by value of products. The manufacturing tax is measured by the value of products. RCW 82.04.220. Rule 201, *supra,* is therefore inapplicable to Reynolds' activities as a manufacturer.

Reynolds contends that, since the reduction of alumina to metal aluminum is only one step in the manufacturing of the finished product of aluminum, it is entitled to apportionment of the tax base according to value attributable to manufacturing in Washington, under the chapter. We disagree. The statute allows deductions only as to "Amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States." Reynolds relies on *Crown Zellerbach Corp. v. State, supra,* 45 Wn.

2d 749. This same argument was raised in *Crown Zellerbach Corp. v. State*, 53 Wn.2d 813, 328 P.2d 884 (1958). We there said, in distinguishing *Crown Zellerbach Corp. v. State*, 45 Wn.2d 749:

> ". . . Appellant cites this decision [45 Wn.2d 749] in support of its contention that apportionment is proper, under the facts of the instant case.
>
> "We do not agree that the cited case so holds because (1) the issue here presented was not before the court in that case, and (2) the apportionment referred to therein concerns activities which are substantially a part of the taxable incident, rather than those activities which enhance only the measure of the tax."

The instant case does not concern activities of Reynolds outside the state. The only taxable incident is Reynolds' manufacturing activity in this state. The gross value of the product manufactured is the measure of the tax only, which is imposed strictly upon the local activity. To make deductions for out-of-state costs would violate RCW 82.04.070, which excludes such deductions from the measure of the tax imposed. *Crown Zellerbach Corp. v. State, supra*, 53 Wn.2d 813. See *St. Regis Paper Co. v. State*, 63 Wn.2d 564, 388 P.2d 520 (1964).

Reynolds contends that the tax imposed offends the Fourteenth Amendment to the Federal Constitution and Art. 1, §3, of our state Constitution. It argues that since the tax is on the value of the manufactured article, it imposes a tax on extraterritorial activities and values. We discussed this argument at length in *Crown Zellerbach Corp. v. State, supra*, 53 Wn.2d 813, wherein we stated:

> "A review of the Federal cases concerned with

> the power of a state to tax a purely local activity, measured by the gross receipts from sales of the product within and outside the taxing state, reveals that such taxes have been upheld, where the local taxable incident is one of sufficient substance so that the sales price substantially reflects the value of the products at the place of manufacture. (Cases cited.)"

The United States Supreme Court in a recent case arising from this state, *General Motors Corp. v. Washington*, 377 U.S. 436, 84 S.Ct. 1564, 12 L.Ed.(2d) 430 (1964), stated the test to be as follows:

> ". . . We must determine whether it is so closely related to the local activities of the corporation as to form 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.' . . ."

Here, the tax on Reynolds is for a purely local activity. Neither the Fourteenth Amendment to the Federal Constitution nor Art. 1, §3 of our state Constitution is contravened.

Reynolds further contends that since the tax imposed is not apportioned, it places a multiple burden upon, or directly interferes with, interstate commerce, in violation of the Commerce Clause of the Federal Constitution, Art 1, §8, Clause 3. This argument is answered by our holding in *Crown Zellerbach Corp. v. State, supra*, 53 Wn.2d 813. The tax on the local activity of manufacturing does not transcend state lines.

Reynolds contends the tax imposed denies it equal protection of the laws in contravention of the Fourteenth Amendment to the Federal Constitution and Art 1, §12, of our state Constitution. It argues that by having an

out-of-state integrated business concern manufacturing in the state of Washington, it is discriminated against in favor of a completely local integrated business concern manufacturing in the state of Washington, in that Reynolds is subject to a multiple tax burden, whereas the local integrated business pays only one tax.

The argument is without merit. There is only one tax imposed on the local manufacturing activity within the state of Washington, which applies the same to all persons engaged in such activity. *Crown Zellerbach Corp. v. State, supra,* 53 Wn.2d 813; *Crown Zellerbach Corp. v. State, supra,* 45 Wn.2d 749.

Regarding the recovery of cryolite, the trial court found a significant change had been accomplished, when the end product was compared with the original substance before it was subjected to the recovery process. This is supported by the record and constitutes a manufacturing activity within the purview of RCW 82.04.120. *Continental Coffee Co. v. State,* 62 Wn.2d 829, 384 P.2d 862 (1963). The reasoning for the imposition of the manufacturing tax on metallic aluminum applies equally to cryolite.

We find it unnecessary to discuss the other arguments of Reynolds in view of our disposition of this appeal.

We hold the taxes imposed by the Washington State Tax Commission in the instant case to be valid. The judgment is affirmed.

HUNTER, J.

We Concur:

ROSELLINI, C. J.
HILL, J.
DONWORTH, J.
FINLEY, J.
WEAVER, J.
OTT, J.
HAMILTON, J.
HALE, J.

APPENDIX "B"

Trial Court's Oral Decision

THE COURT: Plaintiff seeks a refund from taxes paid under Manufacturers Category of the Business and Occupation Tax which is R.C.W. 82.04.240. The year 1955 is used as the example for consideration and all computations and other matters occurring in the record refer to that year and the tax imposed as for that year.

Now, I relied for the facts in this case upon the proof which was taken in this court and not upon any factual statements in the briefs of either party and my summary of the facts I believe will be confined solely to that so far as memory will serve.

Reynolds Metals Company mined bauxite ore, ships it from mines to plants or plants outside of the State of Washington where the ore is changed to alumina. When this process is completed, there is produced a powdery substance which is shipped in railroad cars to Longview, Washington. At Longview, Washington, this powdery substance is subjected to a process by which is produced a metallic aluminum and pigs or ingots of metallic aluminum result from what is done at Longview, Washington.

From Longview, Washington, the pigs or ingots of the metallic aluminum are shipped to various fabricating plants of plaintiff outside of the State of Washington where various articles composed of metallic aluminum are produced.

The State of Washington has taxed the production of this metallic aluminum which takes place at Longview,

Washington, and under the provision of R.C.W. 82.04.240 contention of plaintiff, as I understand it, is that the whole chain of events which have been described as an integrated process for the production of fabricated articles of metallic aluminum because of that the plaintiff contends, as I understand it, that manufacturing does not take place at Longview. Stated more specifically that the conversion of alumina to metallic aluminum at Longview does not constitute manufacturing under the appropriate provisions of our Business and Occupation Tax and particularly under the Manufacturing Category. Consistent with that theory the plaintiff asks that either it be held that manufacturing does not take place at Longview or if contrary-wise it does take place at Longview, that the tax should be apportioned to take account of the costs and charges that have occurred in the total process of production up to the time that metallic aluminum results at Longview.

I think the answer to this contention must be found strictly in application of the statute itself. I do not find any statute and I am referring now to all of the provisions that have been cited to me as well as R.C.W. 82.04.240, any authority for splitting up a process of manufacture into its several parts; and stated another way, what does occur at Longview is manufacture or manufacturing. It was said in *Crown Zellerbach Corporation v. State of Washington*, 53 Wn.2d 813, quoting from page 815 as follows: "Since the statute (R.C.W. 82.04.240) does not define 'To manufacture' to include executive functions, the word 'manufacture' must be given its plain and ordinary meaning." And they cite cases.

"To 'manufacture' is defined in Webster's New International Dictionary Second Edition as follows: 'To make (wares or other products) by hand, by machinery, or by other agency; to work, as raw or partly wrought materials, into suitable forms for use; to fabricate; to invent; also, to produce mechanically.'

"It is the local activity of converting raw materials into a finished product (manufacturing) which is taxed. R.C.W. 82.04.070, *supra*, excludes any deduction from the gross proceeds of sales for the cost of property sold, the cost of materials used, labor costs, and so forth."

Now what we have been asked to do here is tantamount to this. We are asked to construe this statute in such a way as to say that where there are several steps in the process of manufacture; that first, we cannot tax an intermediate step as being manufacturing; or in the alternative, that if a tax is applied to one of the intermediate steps, the costs that have accrued up to that time must be apportioned. To so hold would be an obvious exercise of judicial legislation. There is no support in the statute for so doing and the Court must decline to do it. The language of the statute is plain—we find an exception created, it must be by an act of the legislature and not by judicial decision.

Now, reference has been made in argument to a recent decision of this Court announced from the bench in the case of *Fiberboard Paper Products Corporation*, plaintiff, *versus The State of Washington* and *Charles W. Hodde, Clark Squire* and *G. Merton Dick*, defendants, No. 3307. I am reluctant to comment upon that oral decision which I made from the bench because of the following: That

case has not yet resulted in any findings of fact, conclusions of law and decree and, of course, the rule in this state is well settled that an oral decision by the Trial Judge does not have any dignity of a decision until appropriate findings, conclusions and decree are entered. I feel I must comment, however, because counsel apparently placed some reliance on that case.

It is not in any way apposite in facts to the case at bar. The facts of the *Fiberboard* case briefly were these and they are unusual and significant. Fiberboard takes orders for containers of various sorts which are fabricated into fiberboard over a large area outside of the State of Washington. It has two plants within the State of Washington for the production of fiberboard. One located at Sumner, Washington, and one located at Port Angeles, Washington. According to the stipulated facts it never manufactured any fiberboard until it has an order in hand for a particular type of container which the order calls for. When a firm order is received an appropriate interdepartment order is issued from the headquarters of the company directed to either the plant at Port Angeles or the plant at Sumner for the production of the appropriate type and quality of fiberboard to be used in the container for that particular order. Then and only then do the plants at Port Angeles or Sumner produce the fiberboard. At no time is fiberboard taken out of stock for the filling of an order.

I think the statement of the facts that I have made will at once distinguish the factual pattern from that of the case at bar. I was careful in this decision to point out that

the determination made was strictly limited to the stipulated facts and it follows, of course, that any statements of law made in that opinion were appropriate to these particular facts. Along toward the end of the oral opinion and after summarizing the considerable history of the case upon this general proposition that has been determined by the Supreme Court of the United States, I made a comment which I think has been misconstrued. It refers to the matter of apportionment.

It is contended by the state in this case and if my memory serves me, was also contended in the *Fiberboard* case: That the provisions of R.C.W. 82.04.460 which deals with apportionment are applicable only to the service classification. I did not pass upon that point in the *Fiberboard* case and the only sentence that I used which apparently has been the cause of the misunderstanding of my meaning is the following on page 14: "The contention, if I understand it, is that this is not the sort of apportionment that the courts have been talking about repeatedly."

I may not have made my meaning entirely clear, but the apportionment that I was talking about was the apportionment that the Supreme Court of the United States has come back to repeatedly where they have said that where the fact pattern was such that an apportionment was called for that there the tax act would fail unless it provided for an apportionment. I do not believe we reached the matter of apportionment at all in the case at bar because as I have previously said my reading of the statute convinces me that what happens at Longview is manufacture. The state has a right to tax that

which is an activity occurring entirely within the State of Washington and that no apportionment is called for under any provision of the statute which I am aware of.

Now, many constitutional questions have been raised in this case and without prolonging the matter, they have all been disposed of on factual pattern which was essentially the same as that presented in the case at bar with the single matter of an integrated or progressive process of production. As I have said before, I do not believe that that is material or proper consideration for the Court in this case under the construction of the application of the statute; therefore, the constitutional questions raised have been all fully and adequately disposed of in the first and second *Crown Zellerbach* cases where the decisions of the Supreme Court are relied upon, upon all of these matters.

The first *Crown Zellerbach* case is *Crown Zellerbach Corporation versus The State of Washington* found in 45 Washington (2d), 749; and the second *Crown Zellerbach* case of which I have already referred to is *Crown Zellerbach Corporation versus The State of Washington*, 53 Washington (2d), 813.

I think what I have said disposes of the matter.

APPENDIX "C"

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

REYNOLDS METALS COMPANY, *Appellant,* v. THE STATE OF WASHINGTON, and WILLIAM HODDE, Chairman, CLARK SQUIRE and G. MERTON DICK, members of the WASHINGTON STATE TAX COMMISSION, *Respondents.*	REMITTITUR No. 33597 Thurston County

This is to certify that the opinion of the Supreme Court of the State of Washington filed on March 18, 1965, became the final judgment of this court in the above entitled case on April 19, 1965. This cause is remitted to the superior court from which the appeal was taken for further proceedings in accordance with the attached true copy of the opinion.

Pursuant to Rule 55 on Appeal, costs are taxed as follows:

Two Hundred Eighty-seven and 29/100 ($287.29) Dollars in favor of respondents and against appellant and its surety Federal Insurance Company.

cc: Court Reporter
Williams, Lanza, Kastner & Gibbs
Mr. Dewitt Williams
Hon. John J. O'Connell
Mr. James A. Furber
Mr. Henry W. Wager

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the seal of said Court at Olympia, this 20th day of April, A.D. 1965.

s/William M. Lowry

WILLIAM M. LOWRY
Clerk of the Supreme Court, State of Washington.

APPENDIX "D"

STATUTES
CHAPTER 82.04 of the REVISED CODE OF WASHINGTON

82.04.220—*Business and occupation tax imposed.* There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be. (c 15 § 82.04.220.)

82.04.240—Upon every person except persons taxable under subsection (2) of RCW 82.04.260[1] engaging within this state in business as a manufacturer; as to such persons the amount of the tax with respect to such business shall be equal to the value of the products, including by-products, manufactured, multiplied by the rate of one-quarter of one percent.

The measure of the tax is the value of the products, including byproducts, so manufactured regardless of the place of sale or the fact that deliveries may be made to points outside the state.

82.04.270—Upon every person except persons taxable under subsection (1) of RCW 82.04.260[2] engaging within this state in the business of making sales at wholesale; as to such persons the amount of tax with respect to such business shall be equal to the gross proceeds of sales of such business multiplied by the rate of one-quarter of one percent.

1. This subsection deals with flour manufacturing.
2. This subsection deals with wholesalers of grain.

82.04.440—prior to amendment in 1950. *Persons taxable on multiple activities.* Every person engaging in activities which are within the purview of the provisions of two or more paragraphs (a), (b), (c), (d), (e), (f), and (g) of section 4, shall be taxable under each paragraph applicable to the activities engaged in: Provided, however, That persons taxable under paragraphs (a) or (b) of said section shall not be taxable under paragraphs (c) or (e) of said section with respect to making sales at retail or wholesale of products extracted or manufactured within this state by such persons.[3]

• • • • •

82.04.440—amendment in 1950. *Persons taxable on multiple activities.* Every person engaged in activities which are within the purview of the provisions of two or more of paragraphs (a), (b), (c), (d), (e), (f), and (g) of section 4, shall be taxable under each paragraph applicable to the activities engaged in: Provided, however, That persons taxable under paragraphs (c) or (e) of said section shall not be taxable under paragraphs (a), (b), or (d) (2) of said section with respect to extracting or manufacturing of the products so sold.[3]

• • • • •

3. Paragraph (a) imposed the tax on the business of "extracting" and paragraph (b) imposed the tax on the business of "manufacturing." Persons taxable as extractors or manufacturers were exempt under this section from the retailer's tax imposed by paragraph (c) and from the wholesaler's tax imposed by paragraph (e).

APPENDIX "E"

UNITED STATES CONSTITUTION

Art. I, Sec. 8, clause 3:

"The Congress shall have Power—

• • •

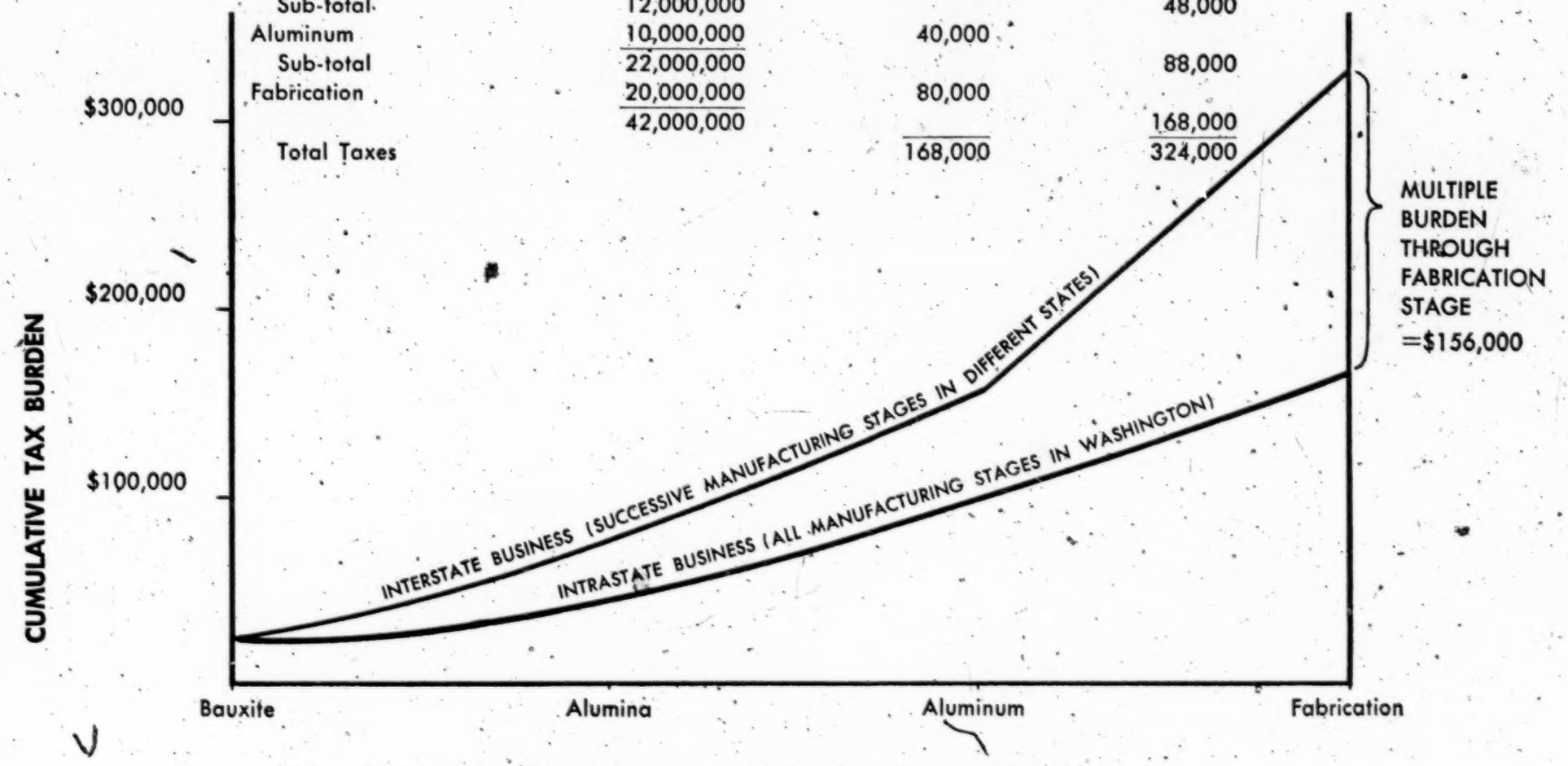
"To regulate Commerce . . . among the several States . . ."

Fourteenth Amendment, Sec. 1:

". . . nor shall any state deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

COMPARISON OF CUMULATIVE TAXES ON INTERSTATE AND INTRASTATE BUSINESS

Stage	Bases	Cumulative Tax at .004 Intrastate	Interstate
Bauxite	5,000,000	20,000	20,000
Alumina	7,000,000	28,000	
Sub-total	12,000,000		48,000
Aluminum	10,000,000	40,000	
Sub-total	22,000,000		88,000
Fabrication	20,000,000	80,000	
	42,000,000		168,000
Total Taxes		168,000	324,000



Notes: 1. Assumes each state assesses unapportioned tax at same rate and base.

2. Curves reflect cumulative tax attributable to each stage, though collection not made until completed or transferred outside state.